

Rural Telephone Coalition

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**FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of)

Common Carrier Bureau Seeks)
Further Comment on Specific)
Questions in Universal Service)
Notice of Proposed Rulemaking)

CC Docket No. 96-45
[DA 96-1078]

**COMMENTS OF THE
RURAL TELEPHONE COALITION
(NRTA, NTCA, OPASTCO)**

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PUBLIC NOTICE

**Federal Communications Commission
1919 M St., N.W.
Washington, D.C. 20554**

**[DA 96-1078]
Released July 3, 1996**

COMMON CARRIER BUREAU SEEKS FURTHER COMMENT ON SPECIFIC QUESTIONS IN UNIVERSAL SERVICE NOTICE OF PROPOSED RULEMAKING

CC DOCKET 96-45

Comment Date: August 2, 1996

On March 8, 1996, the Commission adopted a Notice of Proposed Rulemaking (NPRM) that sought comment on the Congressional directives set out in Section 254 of the Telecommunications Act of 1996 (1996 Act) and that established a Federal-State Joint Board to recommend changes to our regulations to implement Section 254 of the 1996 Act. Specifically, the NPRM asked for comment on: 1) goals and principles of universal support mechanisms; 2) support for rural, insular, and high-cost areas and low-income consumers; 3) support for schools, libraries, and health care providers; 4) enhancing access to advanced services for schools, libraries, and health care providers; 5) other universal service mechanisms; and, 6) administration of support mechanisms.

Comments and Reply Comments in this proceeding were received on April 12, 1996 and May 7, 1996, respectively. Having reviewed the submissions, the Common Carrier Bureau, at the request of the staff of the Federal-State Joint Board, seeks further comment on specific issues relating to the subjects previously noticed in this proceeding. Interested parties are invited to file comments on the attached list of questions. Commenters should restate and underline each question above their responses. Commenters also must provide a brief summary of their comments, not to exceed three sentences per question or three single-spaced pages in total, as a preface to their comments. The comments and comment summary should follow the order of the questions. Comments should be filed on or before August 2, 1996. Interested parties must file an original and four copies of their comments with the Office of the Secretary, Federal Communications Commission, Room 222, 1919 M Street, N.W., Washington, D.C. 20554. Comments should reference CC Docket No. 96-45. Parties must also serve comments on the Federal-State Joint Board and Joint Board staff in accordance with the attached service list.

Parties should send one copy of their comments to the Commission's copy contractor, International Transcription Service, Room 140, 2100 M Street, N.W., Washington, D.C. 20037. Comments will be available for public inspection during regular business hours in the FCC Reference Center, Room 239, 1919 M Street, N.W., Washington, D.C. 20554.

Parties are also asked to submit comments on diskette. Such diskette submissions would be in addition to and not a substitute for the formal filing requirements addressed above. Parties submitting diskettes should submit them to Ernestine Creech, Common Carrier Bureau, Accounting and Audits Division, 2000 L Street, N.W., Suite 257, Washington, D.C. 20554. Such a submission should be on a 3.5 inch diskette in an IBM compatible format using WordPerfect 5.1 for Windows software in a "read only" mode. The diskette should be clearly labeled with the party's name, proceeding, and date of submission. The diskette should be accompanied by a cover letter.

For further information on schools, libraries and health care providers contact:

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-FCC-

Summary

Current rates are generally affordable, but the new law will make major changes in high cost recovery measures, as well as adding more specific universal service standards. Affordable rates remain necessary, but the Act also requires reasonable comparability of rural and urban rates and services, as well as advancing network capabilities. The mechanisms must distinguish between satisfying the Act's principles for low income people and high cost areas, where rates that do not exceed average costs significantly are more relevant than income or subscribership. All recipients of high cost compensation must provide all universal services, although network evolution will require some flexibility for uninterrupted recovery while improvements are deployed.

Schools, libraries and rural health care providers should be compensated for discounts to defined universal services through a separate mechanism that facilitates cost-benefit analysis of this innovative national initiative. The law provides for compensation to any provider required to serve or discount rates for the eligible institutions, but only such providers should participate in the program, with no resale or fees. The program must reimburse or offset the federal obligations of the provider, so block grants to the states would not be lawful. The Joint Board should tailor the program to fulfill the statutory goals, and should not graft on any "needs" testing for the public institutions or the available reimbursements. Again, the law requires sufficient mechanisms based on the enacted principles.

The existing USF and DEM Weighting mechanisms should remain in place. The law will require removal of the cap, as well as contributions from all providers of interstate services. Bulk billing of DEM Weighting amounts would also be salutary, given the interexchange averaging mandate of the Act and current strains caused by the growing gulf between rural and urban

traffic-sensitive charges.

Disaggregation of the high cost recovery in rural LEC territory to target contributions to zones based on density or another factor related to cost differences within even high cost areas would target better -- and would spend the least necessary ratepayer contribution dollars for universal service. For the same reasons, any high cost recovery must be for the ETC's own high costs, since the law requires specific, predictable, explicit and sufficient compensation and prohibits cross-subsidy, and using someone else's costs fails all those tests.

The mechanisms may be different for price cap and rate of return LECs, but each has to satisfy the statutory principles and recovery standards. Proxy costs have been shown not to identify rural LEC costs so far, so the rules should mandate them now or even after a transition for those LECs. The income level and subscribership standards might help with low income programs if proxies are applied to large LECs. Comparability and sufficiency would again be crucial for high cost recovery. Proxy models also have been designed without service quality and infrastructure advancement incentives, notwithstanding the Act's mandates in this regard, and are inherently technologically biased if they rest on an "optimal" theoretical network. Countless waiver proceedings to prevent proxy inaccuracy from denying rural LECs their true costs are not a reasonable cure for requiring an inaccurate proxy in the first place. The specific proxy models are still in flux, preventing adequate evaluation, and have shown little promise for predicting the varying costs of rural LECs.

Competitive bidding will either infringe the states' statutory authority over ETC designation and universal service areas or ensure that only the winning bidder will get specific and sufficient high cost recovery, again in direct violation of the Act. The resulting incentives would discourage both high quality rural service and nationwide advances in capabilities and services.

The CCL is not a subsidy, although some shift to the SLC could be warranted. SLC changes, rebalancing and any other significant changes in end user prices will need to meet the rural-urban comparability and affordability standards, as well as the whole list of principles in the law. The CCL could be improved by bulk billing to correct the uneconomic results and incentives caused by usage sensitive recovery of this portion of loop costs.

Rural Telephone Coalition Comments:

Definitions Issues

1. Is it appropriate to assume that current rates for services included within the definition of universal service are affordable, despite variations among companies and service areas?

“Affordability” is a term new to the Communications Act, and with little legislative history. The concept however is intended to build upon the policies first made explicit by the Commission when it adopted the first Universal Service Fund rules, i.e. that an explicit mechanism should recover enough of the cost of providing dialtone so that basic local service rates do not become unaffordable. Affordability analysis is not limited to evaluating effects on the economically underprivileged, but is to be gauged against the economic burden on the average citizen. The 1996 Act explicitly preserves the Lifeline program, which would be unnecessary if the affordability criteria were meant to limit universal service support to persons presently supported by those programs.

In this context, and in light of the record of the subscribership docket (CC 95-115) indicating that in most cases the level of local service rate is not a material cause of non-subscribership, it is reasonable to conclude that, on average, rates can be considered affordable today.

Because the Commission has not yet defined the services to be supported by the federal universal service support mechanism, the question cannot be answered definitively. However, the record shows that this area is not one of substantial disagreement in regard to services provided to residential and small business subscribers. This conclusion cannot be made in regard to schools, libraries and health care providers until the services to be supported are identified.

In implementing the 1996 Act and judging what is ‘affordable,’ the Joint Board needs to recognize that the national policy mandate deals with several different universal service concerns. These distinct concerns include (1) the problem of people who lack the income to subscribe to and use telecommunications services and (2) the separate problem of ensuring a nationwide public switched network that makes available advancing capabilities and services on terms that encourage the average customer to subscribe to and use the network. The second focuses on areas where relatively sparse population and below-average traffic volumes cause above-average service costs.¹

The universal service objectives of “just, reasonable and affordable rates,” § 254(b)(1) and (I), and reasonably comparable services and rates, § 254(b)(3), apply to all universal service concerns, along with the remaining principles. But differing emphases and interpretations with respect to the governing principles are appropriate depending on what particular concern is under consideration. For example, the policy of “affordable” rates is of paramount importance to ensuring universal service to low income customers. The Act states that it does not affect the current programs to provide service to the needy, § 254(j). However, the Joint Board and FCC may choose to improve those programs to resolve the concerns with unserved groups expressed in the NPRM. Even for the low income mechanisms, moreover, the law’s implicit assumption that universal service is a necessity requiring government intervention may well indicate that some subscribers feel compelled by safety or health or other needs to take service, even if the price is a major burden.

¹ Other distinct universal service interests addressed in the Act involve meeting the special needs of schools, libraries and rural health care providers and of handicapped customers.

While the “just, reasonable and affordable rates” mandate is important for high cost rural areas, Congress also established that rural and urban rates and services must be “reasonably comparable” and that all should have access to “advanced telecommunications and information services,” § 254(b)(2). Congress specified that universal service cost recovery payments should be “sufficient” to “achieve the purposes of this section.” The Conference Report also cautioned that the then on-going universal service review (which was dedicated to reducing the size and controlling the growth of the programs) was not an appropriate foundation for implementing § 254.² There will also be changes as the Joint Board works toward a fully explicit funding mechanism. With all of these instructions and admonitions, it would be imprudent to presume that “affordable” rates should be the primary issue. While the Act requires that all universal services be “affordable,” it nowhere authorizes the Joint Board or the FCC to convert the high cost compensation mandate into a welfare program.

The Joint Board should concern itself, as Congress has directed, with achieving all the attributes of universal service embodied in § 254. Since the rural rates and services must be comparable to those in urban areas, and the question admits the variance in rates, a more fruitful focus for high cost areas would be on parity and infrastructure development incentives.

2. To what extent should non-rate factors, such as subscribership level, telephone expenditures as a percentage of income, cost of living, or local calling area size be considered in determining the affordability and reasonable comparability of rates?

The first three “non-rate” factors -- subscribership level, telephone expenditures as a percentage of income and cost of living -- are relevant to judging “affordability” in connection

² P. 131, Joint Explanatory Statement of the Committee of Conference.

with universal service mechanisms for low income customers. These can provide some insight into whether consumers consider themselves able to pay the price of the monthly fixed charge for the level of service they obtain, what monthly part of their income subscription consumes and how overall prices in their areas compare to other areas. However, the current reliance upon eligibility for other state low income programs to establish eligibility for Lifeline is simpler, less costly to administer and benefits from each state's expertise about its own economic conditions and citizens.

These first three factors are not useful in determining the "reasonable comparability of rates." The question of comparability concerns the level of the rates for similar services in rural and urban areas. Straining to read the comparability mandate as meaning comparably affordable would add nothing to the basic issue of whether a customer has the means to take service. It matters nothing to the needy family struggling to pay even a subsidized telephone that he lives in an affluent county or town or that rates are even higher somewhere else. Affordability is necessarily a household or individual low income issue.

In contrast, the policy of rate and service comparability relates to the concept of a nationwide public switched network available everywhere on the same (or nearly the same) terms. It proceeds from recognition that the marketplace does not provide the same infrastructure investment incentives or per-customer costs where traffic volumes are low and loops are long, but that society will benefit from greater parity of telecommunications opportunities. Low income programs alone will not modernize the rural infrastructure.

Comparability requires that the units of comparison be sufficiently similar. Therefore, the size of the local calling area is relevant to both "comparability" and "affordability." Paying \$20

for flat rate local service in a rural place where a local call can reach a few hundred or a couple of thousand lines is not comparable to paying that monthly rate to reach millions or hundreds of thousands of other lines. The local rate in a rural area may not even cover routine or emergency calls. This restricted service also means that customers in a small calling scope or area must make more toll calls, so that their local rates alone are a poor indicator of “affordability.”

3. When making the "affordability" determination required by Section 254(I) of the Act, what are the advantages and disadvantages of using a specific national benchmark rate for core services in a proxy model?

In order to respond, the “benchmark” must be defined in relation to the other elements of cost recovery, since it has been used differently by the proponents at different times. If the benchmark identifies those costs which are not recovered through the new universal service fund, meeting the statutory requirement for affordability depends therefore on how much of this remainder is recovered through end user charges, e.g., local service and subscriber line charges. Comparability is also a requirement. Thus, a benchmark set to produce high cost recovery beyond a nationwide average could be a useful objective for examining comparability and affordability for the average customer. However, the differences in local and toll rate structures, service quality, local calling scope, etc., would make a meaningful single benchmark impractical to construct.³

As the RTC discussed in the record and will discuss briefly below (see questions 34-48)

³ The RTC assumes that the question is using “core services” as a synonym for “universal services” defined pursuant to § 254(c). The Act does not provide for a distinct universal service category of “core services,” although it allows a separate definition for schools, libraries and rural health care providers and allows a state to adopt and fund a broader universal service definition, § 254(f).

and more extensively in response to the Request for comments about current proxy proposals due August 9, 1996, the proxies proposed so far have not been adequate as surrogates for rural telephone company costs. Any proxy model would need sufficient validation to demonstrate that it would not cause under- or over recovery for rural LECs. Validation is particularly crucial when proxy use is proposed for identifying what costs may be recovered or for setting prices.⁴

4. What are the effects on competition if a carrier is denied universal service support because it is technically infeasible for that carrier to provide one or more of the core services?

There is only one reason consistent with the Congressional intent and the statute for temporary delay of the requirement to provide all universal services throughout the designated service area. This situation will be created by the ongoing implementation of the statute: The law requires an evolving definition of universal service, which necessarily means that the definition may be beyond what some LECs are capable of providing when the definition is adopted or expanded.

In that case, it would defeat the network advancement purposes of the Act unless the eligible telecommunications carrier could continue to receive high cost compensation while it upgrades to meet the requirements of providing all universal services in the entire service area.⁵ The role of the state in determining eligible carriers under § 214(e) set out in the law makes it

⁴ The RTC has suggested that a formula will be necessary to disaggregate high cost compensation. Such a formula is different because it would apply only to allocate the actual costs of a company into cost, density or distance zones, concepts which have been used in past ratemaking by some LECs.

⁵ Consistent with this position is the case in which a non-facilities based carrier “resell” universal services until the facilities-based carrier upgrades its network to accommodate the required services. This would also be true in the case of a qualifying carrier that seeks to use infrastructure sharing to satisfy its eligible carrier status requirements.

possible for this specific issue to be resolved by agencies familiar with the local conditions.

Aside from that, no exception is lawful. Congress has legislated the requirements and conditions attached to gaining and relinquishing essential telecommunications carrier (ETC) status in § 214(e). The provision requiring a state public interest finding before an additional ETC can be designated in a rural telephone company study area, § 214(e)(2), amply demonstrates Congress's concern about the impact of competition -- and particularly subsidized competition -- in such rural areas.⁶ Beyond that, the Act generously permits a CLEC that wants to become an ETC but cannot provide all the required universal services on its own facilities to meet the rest of its universal service obligations using resale. Accordingly, Congress has determined that having to qualify in full as an ETC either does not conflict with the Act's overall pro-competition thrust or is nevertheless justified by the needs of rural LECs' markets.

5. A number of commenters proposed various services to be included on the list of supported services, including access to directory assistance, emergency assistance, and advanced services. Although the delivery of these services may require a local loop, do loop costs accurately represent the actual cost of providing core services? To the extent that loop costs do not fully represent the costs associated with including a service in the definition of core services, identify and quantify other costs to be considered.

The definitions for universal services proposed in the record and the evolution contemplated by the Act, § 254(c), will require universal service contributions to switching and transport costs as well as loop costs. Some implicit high cost compensation that will presumably have to be made explicit already recovers such non-loop costs. For example, the Joint Board should provide high cost compensation for access charges that cause significant disparities between rural and urban areas. This approach would facilitate the toll rate averaging required by

⁶ See also, § 253(f).

§ 254(g) and promote rural long distance competition. It will also be necessary to provide compensation for any network upgrades, such as the software, and even hardware, that rural telephone companies within the top 100 MSAs will have to develop and install to provide number portability -- even if they have no bona fide request and thus no customer to pay the costs.

Schools, Libraries, Health Care Providers

6. Should the services or functionalities eligible for discounts be specifically limited and identified, or should the discount apply to all available services?

Discounts are required to be available for any “universal service” according to Sec. 254(h)(1)(B). Of course, this will depend upon the definition of “universal service.”

7. Does Section 254(h) contemplate that inside wiring or other internal connections to classrooms may be eligible for universal service support of telecommunications services provided to schools and libraries? If so, what is the estimated cost of the inside wiring and other internal connections?

The universal service provision for schools, libraries and rural health care providers requires discounts and mandatory provision related to telecommunications services. Inside wiring has been deregulated, so it will presumably not be declared a “universal service” eligible for discount.

8. To what extent should the provisions of Sections 706 and 708 be considered by the Joint Board and be relied upon to provide advanced services to schools, libraries and health care providers?

The provisions of section 708 may accommodate incorporation into the separate fund for provision of advanced services to schools, libraries and health care providers, but is not likely to be sufficient by itself. Section 706, a provision that addresses advanced telecommunications

incentives, doesn't ensure that funding be available and that schools, libraries, and health care providers have access to advanced services. Thus, §706 provisions must be applied with caution.

9. How can universal service support for schools, libraries, and health care providers be structured to promote competition?

The statutory provision for discount reimbursements or setoffs to their universal service contribution obligations for all telecommunications carriers, by itself, encourages competition because the customers will be able to choose from among competing providers of discounted services.

10. Should the resale prohibition in Section 254(h)(3) be construed to prohibit only the resale of services to the public for profit, and should it be construed so as to permit end user cost based fees for services? Would construction in this manner facilitate community networks and/or aggregation of purchasing power?

Only entities eligible for the institutional discounts and preferences should be able to participate in any way, including sharing, and no resale for consideration for money or any other thing of value is permissible. Imposing end user fees has the potential for frustrating the intent of Congress by limiting access to the publicly-mandated telecommunications programs required by § 254(h).

11. If the answer to the first question in number 10 is "yes," should the discounts be available only for the traffic or network usage attributable to the educational entities that qualify for the Section 254 discounts?

Not applicable.

12. Should discounts be directed to the states in the form of block grants?

No, the statutory plan is for setoffs or reimbursements to carriers to compensate them for

the discounts provided. There is no contemplation of funds being flowed to any third party, including states.

13. Should discounts for schools, libraries, and health care providers take the form of direct billing credits for telecommunications services provided to eligible institutions?

If “billing credits” refers to the manner in which the discount is reflected in the customer’s bill, the form is irrelevant and need not be regulated. If billing credits means something else, it would be inconsistent with the statutory plan for reimbursement and setoffs for carriers. In any event, there is no need for a “middleman” to add delay and administrative costs to the discount compensation process.

14. If the discounts are disbursed as block grants to states or as direct billing credits for schools, libraries, and health care providers, what, if any, measures should be implemented to assure that the funds allocated for discounts are used for their intended purposes?

The RTC believes that the carriers themselves should receive the reimbursement for the funding. If forced to choose block grants or direct billing credits, the RTC believes that direct billing credits are a better means of ensuring that the money is used for its intended purpose.

The discounts should be direct billing credits for the schools, etc., so that the provider and institution would deal face to face. The provider would have an incentive to limit the discounts to the intended statutory purpose to avoid having its reimbursement or offset denied. The complaint process could also be used for enforcement against abuses.

15. What is the least administratively burdensome requirement that could be used to ensure that requests for supported telecommunications services are bona fide requests within the intent of section 254(h)?

The least burdensome way to limit institutional requests for supported services would be

to define bona fide request with specificity and enforce that limitation through the complaint process.

16. What should be the base service prices to which discounts for schools and libraries are applied: (a) total service long-run incremental cost; (b) short-run incremental costs; (c) best commercially-available rate; (d) tariffed rate; (e) rate established through a competitively-bid contract in which schools and libraries participate; (f) lowest of some group of the above; or (g) some other benchmark? How could the best commercially-available rate be ascertained, in light of the fact that many such rates may be established pursuant to confidential contractual arrangements?

The base service prices for discounts would be the lowest rate available to any non-school, -library or -rural health care provider customer. When such a rate already reflects high cost support, the institutional rate should be applied to the supported rate. When a non-regulated carrier provides a discount, it must furnish sufficient information about its contract and other non-tariffed rates to permit an affected institutional customer to assess if it is not provided a discount from the lowest comparable non-institutional rate.

17. How should discounts be applied, if at all, for schools and libraries and rural health care providers that are currently receiving special rates?

The rates should be grandfathered, unless the institutional user is entitled to an additional discount under the Act. The providing carrier should receive compensation for the actual amount of the discount.

18. What states have established discount programs for telecommunications services provided to schools, libraries, and health care providers? Describe the programs, including the measurable outcomes and the associated costs.

The RTC has insufficient information to respond.

19. Should an additional discount be given to schools and libraries located in rural, insular,

high-cost and economically disadvantaged areas? What percentage of telecommunications services (e.g., Internet services) used by schools and libraries in such areas are or require toll calls?

If the discount from rates that already receive high cost compensation is insufficient to achieve the statutory goals for eligible institutions in one or more of the listed categories, a further discount could be appropriate and could lawfully be compensated from the school, library and rural health care provider support mechanism.

Internet access and intra-school district communications in rural areas are typically beyond the local calling areas.

20. Should the Commission use some existing model to determine the degree to which a school is disadvantaged (e.g., Title I or the national school lunch program)? Which one? What, if any, modifications should the Commission make to that model?

The Commission should not base determinations on the relative neediness of schools, libraries and rural health care providers, but rather on whether the statutory goals will not otherwise be achievable because of specific conditions or costs.

21. Should the Commission use a sliding scale approach (i.e., along a continuum of need) or a step approach (e.g., the Lifeline assistance program or the national school lunch program) to allocate any additional consideration given to schools and libraries located in rural, insular, high-cost, and economically disadvantaged areas?

As it does for all other universal service mechanisms, the Act requires “sufficient” support mechanisms to meet the statutory purposes, § 254(b)(5) and (e). Consequently, the Commission can only adopt a support mechanism if it can conclude that the mechanism will satisfy the Act’s purposes. Sliding scales may be more difficult to administer in some circumstances, but are often

preferable because they avoid large changes in compensation which would otherwise be caused by small changes in the relevant parameters.

22. Should separate funding mechanisms be established for schools and libraries and for rural health care providers?

The mechanism(s) adopted to implement § 254(h) should be separate from the high cost, Lifeline, and TRS mechanisms, at least insofar as any accounts that are maintained of payments and setoffs from universal service contributions and obligations. Since § 254(h) initiates a new and untested type of universal service program, it will be important to monitor its costs for comparison to its benefits. Furthermore, any carrier, not just eligible carriers, will have access to the funding mechanism established for provision of service to schools, hospitals and health care providers for the same reason. It may be wise to require separate rural health care provider, school and library accounts, so that each segment of the new national initiative may be evaluated in this manner. It is also crucial to keep the existing mechanisms separate from the new ones to evaluate the impact, costs and benefits of converting from the current system to fully explicit funding of universal service cost recovery.

23. Are the cost estimates contained in the McKinsey Report and NII KickStart Initiative an accurate funding estimate for the discount provisions for schools and libraries, assuming that tariffed rates are used as the base prices?

The RTC has no basis to evaluate these estimates.

24. Are there other cost estimates available that can serve as the basis for establishing a funding estimate for the discount provisions applicable to schools and libraries and to rural health care providers?

The RTC has no information on such cost estimates.

25. Are there any specific cost estimates that address the discount funding estimates for eligible private schools?

The RTC has no information on such cost estimates.

High Cost Fund

General Questions

26. If the existing high-cost support mechanism remains in place (on either a permanent or temporary basis), what modifications, if any, are required to comply with the Telecommunications Act of 1996?

The existing high cost recovery mechanisms should remain in place on a long term basis (i.e., until they are no longer necessary and effective to satisfy the purposes of § 254.) They should be funded through the broader all-provider contributions requirement in § 254(d) of the new law. In addition, the high cost recovery under DEM weighting should be bulk billed to enable interexchange carriers to satisfy their geographic toll rate averaging obligations, currently under pressure from disparity in NECA and depooled LECs' traffic sensitive access charges. Because of the requirement that the definition of universal services is an evolving one, the Act precludes imposition of a cap.

27. If the high-cost support system is kept in place for rural areas, how should it be modified to target the fund better and consistently with the Telecommunications Act of 1996?

High cost recovery in rural telephone companies' study areas should be disaggregated into zones, using a formula based on density, distance or another cost corollary. The resulting matching of their high cost recovery and the variances of such costs within their study areas will reduce misleading market entry signals that would result if the high cost compensation were uniform throughout the area, causing overcompensation in lower cost portions and under

compensation in higher cost areas.

28. What are the potential advantages and disadvantages of basing the payments to competitive carriers on the book costs of the incumbent local exchange carrier operating in the same service area?

It is unlawful, uneconomic and unfair to base high cost payments to CLECs on the serving ILEC's costs. The Act mandates "specific" federal (and state) high cost compensation to designated ETCs, § 254(b)(5) and (e). Payments to one class of LECs based on costs "specific" to an individual carrier of a different class are not even arguably "specific" to the CLECs. Competitors are allowed to choose to enter only markets where their costs are lower than the serving ILEC's costs. Above-cost (i.e., more than sufficient) payments to CLECs will also violate the Act's mandate for "sufficient" high cost recovery and the § 254(k) prohibition on subsidizing competitive services. The ratepayers who will ultimately pay for universal service contributions, however collected, may not lawfully be forced to bear costs that are not necessary for universal service. In addition, the inevitable result of overcompensating the CLECs in this way will be an unfair competitive disadvantage for the ILEC.

29. Should price cap companies be eligible for high-cost support, and if not, how would the exclusion of price cap carriers be consistent with the provisions of section 214(e) of the Communications Act? In the alternative, should high-cost support be structured differently for price cap carriers than for other carriers?

The Joint Board must implement the universal service policy with the needs of high cost customers in mind, regardless of who serves them. Consequently, this proceeding must find a way to achieve the Act's universal service purposes for all customers in high cost areas. Above all, however, the universal service mechanisms may not lawfully restrict the aggregate high cost

compensation available to the areas served by small and rural ILECs whose regulatory posture demonstrates their greater vulnerability to market and regulatory pressures. The Act's mandate for "sufficient" mechanisms continues to govern whatever approach the Joint Board and FCC apply to either set of ILECs.

30. If price cap companies are not eligible for support or receive high-cost support on a different basis than other carriers, what should be the definition of a "price cap" company? Would companies participating in a state, but not a federal, price cap plan be deemed price cap companies? Should there be a distinction between carriers operating under price caps and carriers that have agreed, for a specified period of time, to limit increases in some or all rates as part of a "social contract" regulatory approach?

Should the Commission adopt rules providing different treatment for price cap companies, the federal tariffing status of such companies should be used. Otherwise there will be endless litigation over whether a particular state plan is or is not a price cap plan.

31. If a bifurcated plan that would allow the use of book costs (instead of proxy costs) were used for rural companies, how should rural companies be defined?

Rural companies should be those defined in the 1996 Act as "rural telephone companies," since that definition was written specifically to recognize the different competitive rules which are appropriate for such companies in reaching the difficult balance between promoting competition and preserving and enhancing universal service.

The RTC supports bifurcation. If actual costs are not to be used for large and urban-centered LECs, they must at least be allowed for companies with hard to serve -- low density or low traffic volume --service areas. Congress has defined the "rural telephone companies" that it determined could need the many rural safeguards enacted in the Act, including:

- (1) the reservation of additional state authority over designating CLECs to receive

support, § 214(e)(2),

(2) a distinct approach to the relevant area for universal service purposes, § 214(e)(5),

(3) extra state authority to set the terms for CLEC entry, § 253(f), and

(4) the automatic initial exemption from, and right to request suspension and modification of, the interconnection provisions designed to “jump start” competition.

This proceeding should use that same statutory definition for any bifurcation plan for high cost recovery mechanisms.

32. If such a bifurcated approach is used, should those carriers initially allowed to use book costs eventually transition to a proxy system or a system of competitive bidding? If these companies are transitioned from book costs, how long should the transition be? What would be the basis for high-cost assistance to competitors under a bifurcated approach, both initially and during a transition period?

If rural telephone companies are allowed to use actual costs, which the RTC believes is necessary under both the plain language of the Act and its public policy mandate, they should be permitted to use actual costs for the foreseeable future. If a proxy methodology of proven validity for predicting these carriers’ costs is found, that could justify a transition.

33. If a proxy model is used, should carriers serving areas with subscription below a certain level continue to receive assistance at levels currently produced under the HCF and DEM weighting subsidies?

A proxy model should not be used for rural telephone companies unless and until a valid proxy is found and proven accurate. An accurate, valid proxy must have been shown to predict with reasonable certainty the costs to serve a given LEC’s area. A non-confiscatory proxy plan which uses forward looking costs, will provide an opportunity to recover embedded costs which exceed the forward looking costs. It is true that there is no protection for such costs in a competitive environment, but neither does the government mandate the rates to be charged, the services which were required to be provided, the facilities required to be deployed, or prohibit

exiting the market. Furthermore, any high cost recovery mechanism should be held to the full comparability and other universal service principles of § 254. As explained in the answers to questions 1 and 2, high cost compensation cannot be evaluated or targeted on the basis of subscribership; that function is the job of the Lifeline Assistance program, which Congress found unnecessary to change in § 254(j).

Proxy Models

34. What, if any, programs (in addition to those aimed at high-cost areas) are needed to ensure that insular areas have affordable telecommunications service?

The high cost and low income (i.e., Lifeline and Link-Up) mechanisms, if properly designed to be “sufficient to achieve the purposes of this section, § 254(e), should be sufficient to provide for universal service to insular areas. The need for comparable and affordable interexchange service should be adequately met by implementation of the geographic toll rate averaging requirements of § 254(g). Inclusion of insular areas in the universal services mandate is another reason to reject any proxy methodology absent proof that it is a valid predictor of the costs of serving rural, remote and insular areas.

35. US West has stated that an industry task force “could develop a final model process utilizing consensus model assumptions and input data.” US West comments at 10. Comment on US West's statement, discussing potential legal issues and practical considerations in light of the requirement under the 1996 Act that the Commission take final action in this proceeding within six months of the Joint's Board's recommended decision.

The law does not require the Joint Board to resolve every issue within the initial fifteen months allowed for this proceeding, § 254(a). The speculation that a consensus proxy model may be possible in the future is a patently inadequate basis for the Act’s requirement for “specific,

predictable, and sufficient mechanisms” that are “explicit and sufficient to achieve the purposes of this section,” § 254(d)-(e). The record so far does not demonstrate that any proposal proxy is valid for small and rural telephone LECs.

36. What proposals, if any, have been considered by interested parties to harmonize the differences among the various proxy cost proposals? What results have been achieved?

This information must come from the proponents.

37. How does a proxy model determine costs for providing only the defined universal service core services?

Because the proxy models focus on providing basic voice grade switched service, the major components of which are the loop and switching costs, other proposed universal services would not have a large effect on the cost. In fact, the error range of estimating the vendor switching discounts is probably greater than any incremental software costs of providing additional services. If universal service is defined to include broadband capability, then adjustments to the engineering cost estimates would be required.

38. How should a proxy model evolve to account for changes in the definition of core services or in the technical capabilities of various types of facilities?

See answer to question 37. The RTC may provide further comment in its August 9 filing on the proxy models.

39. Should a proxy model account for the cost of access to advanced telecommunications and information services, as referenced in section 254(b) of the Act? If so, how should this occur?

See answer to question 37.

40. If a proxy model is used, what, if any, measures are necessary to assure that urban rates and rates in rural, insular, and high-cost areas are reasonably comparable, as required in Section